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PAUL NEWMAN,

Commissioner

BRENDA BURNS,

Commissioner

Arizona Corporation Commission

DOCKETED

JAN 23 2012

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IN THE MATTER OF THE APPLICATION )  
OF VAIL WATER COMPANY FOR )  
AUTHORITY TO ISSUE PROMISSORY )  
NOTE(S) AND OTHER EVIDENCE OF )  
INDEBTEDNESS PAYABLE AT PERIODS )  
OF MORE THAN TWELVE MONTHS )  
AFTER THE DATE OF ISSUANCE. )

DOCKET NO. W-01651B-99-0351

IN THE MATTER OF THE APPLICATION )  
OF VAIL WATER COMPANY FOR A RATE )  
INCREASE )

DOCKET NO. W-01651B-99-0406

NOTICE OF FILING TESTIMONY

Attached is the Direct Testimony of Christopher Volpe filed on behalf of Vail  
Water Company.

Dated this 23rd day of January, 2012.

LEWIS AND ROCA

Michael F. McNulty  
Michael Hallam  
Lewis and Roca, LLP  
40 N. Central Avenue  
Phoenix, Arizona 85004  
Attorneys for the Vail Water Company

ORIGINAL and fifteen (15) copies  
of the foregoing filed this 23rd day of  
January, 2012 with:

1 Arizona Corporation Commission  
2 Docket Control – Utilities Division  
3 1200 W. Washington Street  
4 Phoenix, Arizona 85007

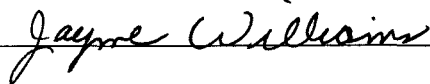
5 COPY of the foregoing hand-delivered  
6 this 23rd day of January 2012, to:

7 Janice Alward, Chief Counsel  
8 Charles Hains  
9 Legal Division  
10 Arizona Corporation Commission  
11 1200 W. Washington Street  
12 Phoenix, Arizona 85007

13 Steve Olea, Director  
14 Utilities Division  
15 Arizona Corporation Commission  
16 1200 W. Washington Street  
17 Phoenix, Arizona 85007

18 COPY of the foregoing  
19 mailed this 23rd day of January, 2012, to:

20 Jane Rodda, Administrative Law Judge  
21 Hearing Division  
22 Arizona Corporation Commission  
23 400 W. Congress St.  
24 Tucson, Arizona 85701

25   
26

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

GARY PIERCE, Chairman  
BOB STUMP  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF )  
VAIL WATER COMPANY FOR AUTHORITY )  
TO ISSUE PROMISSORY NOTE(S) AND )  
OTHER EVIDENCE OF INDEBTEDNESS )  
PAYABLE AT PERIODS OF MORE THAN )  
TWELVE MONTHS AFTER THE DATE OF )  
ISSUANCE. )

**DOCKET NO. W-01651B-99-0351**

IN THE MATTER OF THE APPLICATION OF )  
VAIL WATER COMPANY FOR A RATE )  
INCREASE )

**DOCKET NO. W-01651B-99-0406**

**DIRECT TESTIMONY OF  
CHRISTOPHER VOLPE  
ON BEHALF OF VAIL WATER COMPANY  
JANUARY 23, 2012**

**DIRECT TESTIMONY OF  
CHRISTOPHER VOLPE  
ON BEHALF OF  
VAIL WATER COMPANY  
JANUARY 23, 2012**

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**I     INTRODUCTION AND QUALIFICATIONS**

**Q.     PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND TELEPHONE  
NUMBER.**

A.     My name is Christopher (“Kip”) Volpe. My business address is 1010 N. Finance Center  
Drive, Suite 200, Tucson, AZ 85710, and my business phone number is 520-571-1958,  
ext. 105.

**Q.     BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

A.     I am employed by TEM Corp., a management company that performs management  
services for Vail Water Company (“Vail” or the “Company”) under a service contract.

**Q.     PLEASE DESCRIBE VAIL WATER COMPANY AND ITS BUSINESS.**

A.     Vail is a private water company that provides water to approximately 3,900 customers in  
Pima County, Arizona.

**Q.     PLEASE DESCRIBE YOUR PRIMARY RESPONSIBILITIES FOR VAIL.**

A.     I am a Vice President of the Company and oversee the administration and operations of  
Vail.

**Q.     WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

A.     To address the issues set forth in the Procedural Order dated December 15, 2011.

**II     BACKGROUND INFORMATION**

**Q.     IN DECISION NO. 62450, THE COMMISSION APPROVED A SURCHARGE  
AND HOOK UP FEES TO ALLOW VAIL TO PURSUE THE DIRECT USE OF  
WATER FROM THE CENTRAL ARIZONA PROJECT (“CAP”). WHY IS VAIL  
CONTINUING TO PURSUE THIS DIRECT USE?**

1 A. It was the common understanding in the year 2000, as it is today, that the preferred  
2 course of action with respect to CAP utilization is direct use of CAP within Vail's service  
3 area, rather than CAP recharge, at such time as direct use becomes feasible. Because  
4 Vail's service area is more than 40 miles from the CAP aqueduct, no one envisioned that  
5 the Company would be economically capable of building a stand-alone water  
6 transmission system to provide its customers with CAP water. Rather, it was anticipated  
7 that at some juncture, the CAP's largest customer, the City of Tucson, would expand  
8 eastwards until its delivery systems were sufficiently close to Vail's infrastructure that  
9 Vail could then extend its system to that of Tucson Water, the City's wholly-owned water  
10 utility.

11 As far back as the 1970s, the City of Tucson had envisioned becoming a  
12 wholesale CAP delivery utility, serving other water utilities in the Tucson valley.  
13 However, due to initial problems with the City's CAP treatment facility, Tucson Water  
14 did not wheel CAP water to anyone from 1975 until very recently, notwithstanding that  
15 its service area expanded dramatically over that period, and notwithstanding that its  
16 infrastructure became increasingly accessible to numerous utilities, including to Vail.

17 In 2008, the Mayor and Council of the City of Tucson and the Board of  
18 Supervisors of Pima County agreed to enter into a wide-ranging water policy planning  
19 exercise, reviewing the fundamental changes that would be needed in the Tucson valley  
20 to ensure the community's future. One goal of this planning exercise was enabling  
21 Tucson Water to become a CAP wheeling entity in the Tucson valley. In 2009, Tucson  
22 Water again pursued the difficult job of finding mutually-acceptable ways to become the  
23 entity that transmitted CAP water from the CAP aqueduct to various utilities around the  
24 Tucson valley. Finally, in June 2011, the City of Tucson and the Town of Oro Valley  
25 entered into an intergovernmental agreement for wheeling CAP water that Tucson

1 anticipates will serve as a model for providing similar services to other residential water  
2 utilities in eastern Pima County, including Vail.

3 Following these developments closely, officials from Vail contacted Tucson  
4 Water to ascertain the feasibility of entering into a similar wheeling agreement. The City  
5 of Tucson, having looked forward to serving in this capacity now for some 35 years, was  
6 strongly encouraging, and negotiations between Tucson and Vail began in earnest at that  
7 time. As a means of illustrating the new water policy regime in effect at Tucson Water,  
8 we asked Tucson Water to provide a position statement of its interest in becoming a  
9 wheeling entity for Vail, and were provided with the correspondence from Interim  
10 Director Andrew Quigley dated August 16, 2011, attached as Exhibit A.

11 When the Commission issued Decision No. 62450, Vail's CAP allocation was  
12 786 acre-feet per year. Since that time, Vail's customer base has grown dramatically.  
13 Vail is currently serving approximately 1,100 acre-feet per year and, in anticipation of  
14 future growth, has acquired rights to 1,857 acre-feet per year of CAP water. The benefit  
15 of delivering CAP water directly to Vail's customers is magnified by this increase in  
16 customers and projected future growth, and the corresponding increase in demand within  
17 Vail's service area.

18 **Q. PLEASE DISCUSS THE FINANCIAL ASPECTS OF THE CAP PROJECT FROM**  
19 **VAIL'S PERSPECTIVE.**

20 **A.** From the time the Commission approved the CAP fees in 2000 until October 2011, Vail  
21 has collected a total of approximately \$4.1 million. Over that same period, Vail has spent  
22 approximately \$2.7 million on expenses related to maintaining its rights to the CAP  
23 allocation with the ultimate goal of delivering CAP water directly to its service area. As  
24 a result, and including investment earnings, we have accumulated approximately \$1.9  
25 million of CAP funds for future expenses necessary to complete this project.

1           As required by Decision No. 62450, all of the money collected from CAP fees is  
2       kept in a separate account and can only be used for expenses related to the project. The  
3       bulk of the capital expenses for this project will be incurred over the next few years as we  
4       implement our plans to deliver the CAP water directly to our customers. This is precisely  
5       how the Commission envisioned the CAP fees working -- that is, Vail would accumulate  
6       funds over the first 10-12 years so it would have adequate funds available when the large  
7       capital expenses were incurred. Vail currently projects that all of the accumulated funds,  
8       as well as all additional CAP funds that we collect between now and 2015, will be  
9       required to complete this project and fund annual ongoing CAP and wheeling costs.  
10      Again, this is how the Commission envisioned Vail funding this project when it approved  
11      the fees in 2000.

12   **III     TESTIMONY REGARDING ISSUES SET FORTH IN PROCEDURAL ORDER**  
13   **DATED DECEMBER 15, 2011.**

14   **Q.     WHAT ARE VAIL'S CURRENT PLANS FOR THE DIRECT USE OF CAP**  
15   **WATER IN ITS SERVICE AREA?**

16   A.     Vail still plans to deliver CAP water to its customers by the end of 2015 as required by  
17       Decision No. 62450. Although the original order required the Company to have final  
18       plans by the end of 2010, that is not the critical deadline to the ultimate completion of this  
19       project. On November 8, 2011, Tucson Water's Interim Director Sandy Elder sent Vail a  
20       letter, attached as Exhibit B, outlining the steps that will need to be taken to finalize a  
21       wheeling agreement that will take effect in 2015. As evidenced by the letter, Vail and  
22       Tucson Water have taken significant steps and will continue to take significant steps  
23       toward adoption of a wheeling agreement to allow direct use of CAP water by Vail's  
24       customers.



1 **Q. WHAT ARE THE BENEFITS OF VAIL'S PLAN TO USE CAP WATER**  
2 **DIRECTLY?**

3 A. Direct use of Vail's CAP water will benefit its customers in several ways. First, it will  
4 secure a renewable supply of potable water, fortifying its assured water supply. Direct  
5 access to the CAP water will also enhance Vail's ability to provide an uninterrupted  
6 supply from a source with similar quality to groundwater. In addition to these service  
7 benefits, the direct use of CAP water should be less expensive for Vail's customers in the  
8 long term by maintaining compliance with the management plan of the Tucson Active  
9 Management Area ("AMA") by mitigating Vail's replenishment obligations instead of  
10 purchasing more costly CAGR credits. The project will also relieve pressure on  
11 aquifers in the Tucson AMA and benefit the entire state by firming Arizona's supply of  
12 Colorado River water.

13 **Q. WHAT IS VAIL'S POSITION WITH RESPECT TO REFUNDS?**

14 A. Although Vail, at the suggestion of Commission Staff, offered to refund the CAP  
15 surcharges collected in 2011, Vail does not believe that this is the best approach. As  
16 explained above, all of the money Vail collects as CAP fees must either be used on the  
17 CAP project or refunded at some later date. Any refunds the Commission requires now  
18 will threaten the viability of this beneficial project. At this point, with significant  
19 expenses looming over the next few years, Vail strongly encourages the Commission to  
20 allow Vail to continue collecting the CAP fees and to evaluate the necessity for a refund,  
21 if applicable, after the project is completed.

22 **Q. IS THE CONTINUED USE OF FUNDS FROM THE CAP SURCHARGE AND**  
23 **THE CAP HOOKUP FEES STILL THE BEST PLAN TO FUND DIRECT USE OF**  
24 **CAP WATER BY 2015.**

25 A. Yes.

1 **Q. IS DECEMBER 31, 2015 STILL AN APPROPRIATE DATE BY WHICH TO**  
2 **REQUIRE DIRECT USE?**

3 A. Yes.

4 **Q. DOES VAIL BELIEVE THAT PENALTIES ARE APPROPRIATE IN THIS**  
5 **SITUATION?**

6 A. No. Vail's customers have not been harmed by the failure to meet the deadline to file  
7 plans by December 31, 2010. In fact, Vail's customers have received a benefit by not  
8 paying CAP fees starting in November 2011 and continuing until a final decision in this  
9 proceeding. As noted above, the Company has always planned to meet the ultimate,  
10 critical deadline of Decision No. 62450 -- the direct delivery of CAP water by the end of  
11 2015.

12 **Q. HOW MUCH IN CAP FEES HAS VAIL LOST SINCE IT STOPPED**  
13 **COLLECTING THEM IN NOVEMBER?**

14 A. In November and December, Vail lost approximately \$18,000 in CAP surcharges and  
15 \$9,500 in hook up fees. That is approximately \$14,000 per month, and I expect it to be  
16 roughly the same amount each month until the Commission allows Vail to begin  
17 collecting the CAP fees again. Vail would request guidance from the Commission on  
18 this issue as soon as possible since it will never be able to recover these funds, and, as  
19 already explained, the loss of funds in Vail's CAP account threatens the viability of this  
20 important project.

21 **Q. PLEASE EXPLAIN VAIL'S POSITION WITH RESPECT TO EXTENDING THE**  
22 **DEADLINE FOR SUBMITTING FINAL PLANS TO THE COMMISSION.**

23 A. Vail requests an extension of this deadline until June 30, 2013. Vail takes the  
24 Commission's deadlines very seriously and very much regrets not meeting this deadline.

1 Vail now recognizes that it should have sought an extension prior to December 31, 2010.  
2 As previously explained, it was not possible for Vail to provide "final plans" by  
3 December 31, 2010, due to Tucson Water's internal schedule for wheeling CAP water to  
4 other utilities. Vail explained the situation to Staff beginning in the spring of 2011 and  
5 has been working with Staff since that time in an attempt to comply with the  
6 Commission's order. As evidenced by the recent progress made with Tucson Water, Vail  
7 is confident that it will complete final plans by June 30, 2013, if not sooner, and still meet  
8 the original deadline of December 31, 2015 for direct delivery of CAP water to its  
9 customers.

10 Decision No. 62450 recognized that extensions of the December 31, 2010  
11 deadline might be appropriate upon a showing of good cause (see Conclusion of Law No.  
12 7). For all of these reasons, good cause does exist to extend this deadline until June 30,  
13 2013. Although the Company failed to meet the original deadline, a failure which it very  
14 much regrets, this failure is not a basis to discontinue the progress being made toward the  
15 very important and critical goal of providing direct use of CAP water to Vail's service  
16 area.

17 **Q. PLEASE DISCUSS VAIL'S CAP EXPENSES THAT ARE DUE IN 2012.**

18 A. Vail is scheduled to pay CAP approximately \$254,000 in 2012. The vast majority of this,  
19 approximately \$240,000, is due before Vail takes delivery of its annual CAP allocation.  
20 Delivery occurs in March, April, and May of each year. Payments for these deliveries are  
21 due as follows: \$75,500 on February 20th, \$89,500 on March 20th, and another \$75,500  
22 on April 20th. As a result, Vail respectfully requests that the Commission provide  
23 authorization for Vail to use these funds as soon as possible.

1    **IV    CONCLUSION**

2    **Q.    DOES THIS CONCLUDE YOUR TESTIMONY?**

3    **A.    Yes.**

## **EXHIBIT A**

August 16, 2011



CITY OF  
TUCSON

TUCSON WATER  
DEPARTMENT

Christopher Volpe  
The Estes Company  
1010 N. Finance Center Drive, Suite 200  
Tucson, AZ 85710

Subject: Wheeling CAP Water to Vail Water Company

Dear Mr. Volpe:

Thank you for approaching Tucson Water about wheeling a volume of the Vail Water Company CAP allocation, through our distribution system to your water system. As discussed, our extensive discussions with the Town of Oro Valley helped to identify the critical steps for building a foundation for a wheeling agreement. These steps include:

- Hydraulics analysis of our two water systems and identification of a connection point between them.
- Performing financial calculations of capital and operating costs plus the subsequent generation of a wheeling rate.
- Developing necessary legal documents.
- Construction of the necessary infrastructure to connect the two systems.

With respect to the recently completed wheeling agreement with Oro Valley, which was our first, this process took more than two years. A more complex agreement with the Pascua Yaqui Tribe took five years to complete. Based on the Oro Valley experience, we should be able to do much of it in a shorter timeframe; between six and twelve months.

Shortly, staff will be in contact with you to set up working meetings to begin building this foundation. I look forward to working with the Vail Water Company to complete a mutually beneficial agreement to move a volume of its CAP allocation off the canal, through the Tucson Water system and to the Company's service area.

Very truly yours,

A handwritten signature in dark ink, appearing to read "Andrew H. Quigley".

Andrew H. Quigley  
Interim Director

AHQ/lr

cc: Richard Miranda, Deputy City Manager  
Sandy Elder, Deputy Director, Tucson Water



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## **EXHIBIT B**



CITY OF  
TUCSON  
TUCSON WATER  
DEPARTMENT

November 8, 2011

Christopher Volpe  
The Estes Company  
1010 N. Finance Center Drive, Suite 200  
Tucson, AZ 85710

Subject: Wheeling CAP Water to Vail Water Company – Next Steps

Dear Mr. Volpe:

Thank you for your continued partnership in working with us to determine the requirements and most efficient solutions for Tucson Water (TW) to wheel Vail Water Company's (VWC) CAP allocation through our distribution system. As discussed at our last meeting on September 13, 2011, there are a number of items that still need to be addressed in order for TW and VWC to finalize a "wheeling design" with an ultimate goal of initiating wheeling in CY2015. These items are:

**- Financial** – cost of service, wheeling rates, capital components, etc.

Timeline on financial approval by Mayor and Council for standard water rates was provided after our last meeting. After the cost of service is determined in March 2012<sup>2</sup>, we will have the necessary inputs to proceed with the detailed calculations to determine a wheeling rate to VWC.

POC: Belinda Oden

*Estimated Completion Date: 5/30/2012*

**- Power** – determine initial cost and proposed escalation factor

Parallel to the wheeling rate study, TW has already begun calculation of the power costs required to wheel an acre-foot of water to VWC. Preliminary calculations estimate that today's power cost to wheel VWC water is approximately \$160/AF. As in prior wheeling agreements, TW performs an annual adjustment on the actual power costs to wheel water.

POC: Cecilio Flores

*Estimated Completion Date: 10/31/11*

**- Hydraulic Analysis** – determine infrastructure upgrades and interconnect location

The hydraulic analysis performed to date shows adequate infrastructure capacity to wheel up to 2,000 AF of VWC's CAP allocation to the TW Houghton reservoir. In order to wheel the remaining distance to VWC's closest point of wheeling delivery location, upgrades to the Old Vail Tank site are needed along with a main extension.



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Re: Wheeling CAP Water to Vail Water Company – Next Steps

10/27/2011

Page 2

The construction of the booster upgrades and electrical service is currently planned as part of a developer financed project (Plan Number 096-2008) though no construction activity has taken place by the developer. If VWC were to construct the upgrades, an estimated financial requirement of \$200K is required. Additionally, approximately three miles of 12-inch main, with estimated cost of ~\$1.5M, is required to complete the connection between TW and VWC. Final details on transmission main alignment need to be identified.

POC: Richard Herran

*Estimated Completion Date: 11/30/2011*

**- Finalize Wheeling Parameters** – base or peak load, fire flow, etc.

From prior discussions, it is understood that VWC will receive wheeled water under a base load scenario and that no fire flow will be provided though the wheeling interconnect. Confirmation of these parameters is lynch-pin to arriving at the wheeling rate and sizing infrastructure upgrades necessary to the wheeling.

POC: Sandy Elder and Joe Olsen

*Estimated Completion Date: 11/30/2011*

**- Wheeling Agreement** – approval through respective governing bodies

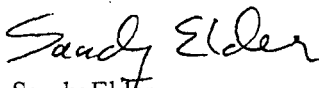
The final step to enacting a wheeling agreement between TW and VWC will be approval of the written wheeling agreement by the respective governing bodies. The wheeling agreement between Oro Valley and TW can serve as a template by which to fine tune based on the aforementioned parameters.

POC: Chris Avery

*Estimated Completion Date: 6/15/2012*

We look forward to continuing to meet with you and your team to finalize the above items. Should you have any questions, please do not hesitate to contact me at 791-2666 or Joe Olsen at 837-2216.

Respectfully yours,



Sandy Elder  
Interim Director

JO/lr

